

IN THE

# Supreme Court of the United States

October Term, 1940

No. 209

CHAPMAN BROTHERS COMPANY, a corporation,

*Appellant,*

vs.

SECURITY-FIRST NATIONAL BANK OF LOS ANGELES,

*Appellee.*

## BRIEF OF APPELLEE IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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**BRIEF OF APPELLEE IN OPPOSITION TO  
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**Statement of the Case.**

It seems to appellee that some of the material facts have been omitted from the Statement of the Case of appellant, or too lightly stressed, and appellee, therefore, deems it advisable to present the following Statement of the Case:

The appellant corporation has a capital stock of \$100,000.00, divided into 100,000 shares of the par value of \$1.00 each, all of said stock being issued and outstanding. There are ten stockholders in this corporation, mainly consisting of members of the Chapman family. [Transcript of Record, Vol. I, pp. 6-7.]

The trial court found that on March 2, 1939, the appellant corporation herein had an unsecured indebtedness of \$29,808.76, and a secured indebtedness of \$2,289,-



530.73, making a total indebtedness of \$2,319,339.49 as of March 2, 1939. [Findings of Fact, XIX, Tr. of Rec., Vol. I, p. 81.]

The secured indebtedness of the appellant corporation is made up as follows:

	Trust Deed Principal Balance	Accrued Interest	Accrued and/or Funded Taxes	Less Deposits for Taxes and Interest	Net Total
Security-First National Bank of Los Angeles: Loans of \$1,800,000.00 and \$50,000.00	\$1,613,201.93	\$ 53,978.16	\$1,353.08		\$1,668,533.17
Security-First National Bank of Los Angeles: Loan of Trust Department	233,496.84	58,414.91	2,334.67	2,100.97	292,145.45
Security-First National Bank of Los Angeles: Loan of Trust Department	108,770.52	12,884.72	767.40	699.03	121,723.61
Security-First National Bank of Los Angeles: Loan on 516 S. Alexandria	8,878.26	60.55	235.80	87.00	9,087.61
Bank of America National Trust and Savings As- sociation:	175,000.00	3,062.50	2,169.50	800.72	179,431.28
California Bank:	17,559.82	395.10	654.69		18,609.61
	<u>\$2,156,907.37</u>	<u>\$128,795.94</u>	<u>\$7,515.14</u>	<u>\$3,687.72</u>	<u>\$2,289,530.73</u>

[Findings of Fact, XVI, Tr. of Rec., Vol. I, p. 78.]  
[Testimony of appellant corporation's auditor, Walter L. Blanton, Tr. of Rec., Vol. II, pp. 8-20.]

The loans of \$1,800,000.00 and \$50,000.00 are secured by a deed of trust with assignment of rentals and leases on eighteen parcels of real property in the city of and county of Los Angeles, state of California, and by a chattel mortgage on personal property located on portions thereof. [Findings of Fact, VI, Tr. of Rec., Vol. I, pp. 63-70, incl, and Findings of Fact, XIV, Tr. of Rec., Vol. I, p. 75.]

The loan of \$1,800,000.00 was executed by appellant corporation as the latest evidence and renewal in part of a long series of indebtedness incurred and owing by it to appellee dating back prior to the year 1925. On December 31, 1925, this indebtedness was \$428,100.00; on December 31, 1926, this indebtedness was \$574,250.00; on December 31, 1927, this indebtedness was \$423,400.00; on December 31, 1928, this indebtedness was \$590,000.00; on December 31, 1929, this indebtedness was \$577,000.00; on December 31, 1930, this indebtedness was \$976,000.00; on December 31, 1931, this indebtedness was \$973,000.00; on December 31, 1932, this indebtedness was \$971,000.00; on December 31, 1933, this indebtedness was \$1,106,906.25; on December 31, 1934, this indebtedness was \$1,137,919.03; on December 31, 1935, this indebtedness was \$1,308,684.97; on December 31, 1936, this indebtedness was \$1,783,022.69; on December 31, 1937, this indebtedness was \$1,595,510.85; and on March 15, 1939, this indebtedness was \$1,613,976.93. [Findings of Fact, VII, Tr. of Rec., Vol. I, pp. 70-74.]

That the interest on the loan of \$1,800,000.00 was paid only to April 5, 1938, plus \$4,531.14 on account of interest accruing thereafter, and that interest on the loan of \$50,000.00 was paid only to June 5, 1938.

That the loan of the Trust Department of the Security-First National Bank of Los Angeles on which a principal balance is due of \$233,496.84 was secured by a deed of trust on a certain garage building [Findings of Fact, XIII, Tr. of Rec., Vol. I, p. 76], and that the interest on said loan was paid only to January 19, 1936, plus \$1,901.19 on account of interest accruing thereafter. [Findings of Fact, XVI, Tr. of Rec., Vol. I, p. 79.]

That the loan of the Trust Department of the Security-First National Bank of Los Angeles on which a principal balance is due of \$108,770.52 was secured by a deed of trust on certain unimproved property [Findings of Fact, XIII, Tr. of Rec., Vol. I, p. 76], and that no interest has been paid on said loan, with the exception of \$349.03, since the date of said loan, to-wit, March 4, 1936. [Findings of Fact, XVI, Tr. of Rec., Vol. I, p. 79.]

That the loan of Security-First National Bank of Los Angeles, on which a principal balance is due of \$8,878.26 is secured by a deed of trust on a certain residence located at 516 South Alexandria street, Los Angeles, California. [Findings of Fact, XII, Tr. of Rec., Vol. I, p. 76.]

That the loan of the Bank of America National Trust and Savings Association, on which a principal balance is due of \$175,000.00, is secured by a deed of trust on three pieces of real property [Findings of Fact, XIV, Tr. of Rec., Vol. I, p. 77], and that said loan was made on April 15, 1933, and that on or about August 15, 1937, the appellant corporation executed and delivered to the said Bank of America its promissory note in the sum of \$17,500.00, which is unsecured, and which was accepted by said bank in payment of interest then due and delinquent on said loan of \$175,000.00, and paid the interest thereon to August 15, 1937, and that the interest on said

loan has been paid to November 15, 1938, and that said \$17,500.00 note has not been paid. [Findings of Fact, XVI, Tr. of Rec., Vol. I, p. 79.]

That the loan of the California Bank, on which there is a principal balance due of \$17,559.82, is secured by a deed of trust covering certain real property, and that interest thereon was paid to October 14, 1938. [Findings of Fact, XV, Tr. of Rec., Vol. I, p. 77; Findings of Fact, XVI, Tr. of Rec., Vol. I, p. 80.]

That the unpaid principal balance of the promissory note for \$1,800,000.00 due appellee includes an advance of \$12,957.24 made by said appellee for the payment of the taxes on property covered by the deed of trust securing said indebtedness, and also includes the further sum of \$20,244.69 advanced by said appellee for the first half of the 1938-39 taxes on said real property securing said indebtedness. [Findings of Fact, XVIII, Tr. of Rec., Vol. I, p. 80.]

That the appellant corporation has shown a continuing loss on its operation since the year 1933, and that such net losses after all charges are as follows:

1934, \$120,924.88; 1935, \$111,279.43; 1936, \$101,778.46; 1937, \$132,317.30; fourteen months preceding March 2, 1939 \$140,957.76. [Findings of Fact, XX, Tr. of Rec., Vol. I, p. 84.]

That, in addition to the foregoing indebtedness, the appellant corporation, Chapman Brothers Company, was, prior to February 20, 1939, indebted to the Transcounties Corporation and the Chapman Acres Trust, in the sum of \$294,741.08, which indebtedness accrued by reason of the payment by said corporations of the guaranty of Charles C. Chapman, in the sum of \$294,782.33, as is set forth in

the findings of fact. [Findings of Fact, XIX, Tr. of Rec., Vol. I, p. 81.] That on February 20, 1939, in connection with this indebtedness the stockholders of Chapman Brothers Company, the appellant corporation, executed the agreement with the Transcounties Corporation and the Chapman Acres Trust set forth on pages 81, 82 and 83 of the Transcript of Record, Volume I.

There has been no attack made by appellant on any of the facts hereinabove recited as set forth in the findings of fact, and they are undisputed.

The officers of the appellee, Security-First National Bank of Los Angeles, and the officers of the appellant, Chapman Brothers Company, throughout 1937 and 1938 conferred together almost continuously relative to plans looking to the improvement of the financial condition of the appellant corporation and its rehabilitation. No solution was found, and on the 26th day of October, 1938, appellee, Security-First National Bank of Los Angeles, a national banking association, commenced proceedings in the Superior Court of the State of California, in and for the County of Los Angeles, for the specific performance of the conditions and covenants of the deed of trust securing its indebtedness, and for the appointment of a receiver. Pursuant thereto, R. E. Allen and G. A. Chapman were appointed receivers *pendente lite*, and took possession of the real and personal property securing the indebtedness owing to the Security-First National Bank of Los Angeles, a national banking association. Thereafter proceedings for the foreclosure of the deed of trust securing said indebtedness were commenced, and a trustee's sale under foreclosure was set for March 4, 1939.

On March 1, 1939, the appellant corporation filed its petition herein for reorganization under Chapter X of the Bankruptcy Act. Thereafter an answer was filed on behalf of appellee, Security-First National Bank of Los Angeles, controverting all of the material allegations of the petition. After a hearing on the issues made by the petition and this answer, the Court rendered its order from which appellant appealed to the Circuit Court.

The Court made its findings of fact, in which it found the foregoing facts to be true, and further found that the reasonable market value of all the assets of the appellant corporation did not exceed \$1,300,000.00, and that the appellant corporation admitted a total liability on March 2, 1939, of \$2,319,339.49. [Tr. of Rec., Vol. I, p. 85.] The Court further found that the liabilities of the appellant corporation exceed its assets by a sum in excess of \$1,000,000.00; that the appellant corporation was hopelessly insolvent. [Tr. of Rec., Vol. I, p. 85.]

The Court further found that it was unreasonable for the appellant corporation to expect that any possible plan of reorganization could be effected, and that the appellant corporation could not evolve a plan of reorganization that would be fair and equitable and that would enable it to pay its creditors in full. [Tr. of Rec., Vol. I, p. 89.]

From its findings of fact the Court concluded that the petition of the appellant corporation was not filed in good faith, and that the material allegations thereof were not sustained by the proofs; that it was unreasonable for the appellant corporation to expect that any plan of reorganization could be effected. Thereupon the Court dismissed the proceedings, and the appellant appealed.

## ARGUMENT.

Appellee will discuss in this brief the following points, under separate headings:

(1) The assignments of error made by appellant in its appeal to the Circuit Court of Appeals did not present any questions for review.

(2) In the absence of an attack, the findings of fact are conclusive upon an appellate tribunal.

(3) The evidence sustains the findings of fact.

(4) The petition of appellant and the evidence adduced in support thereof fail to show that the proceeding is filed and prosecuted in good faith as required by Section 75 of the United States Bankruptcy Act.

(a) The petition fails to disclose any plan of reorganization or possibility of effecting the same.

(b) The appellant corporation's liabilities exceed its assets to such an extent that it shows the possibility of reorganization to be hopeless.

(c) The burden of proof to show a plan of reorganization and the possibility of its being effected is upon appellant, and appellant has failed to sustain this burden by competent evidence.

(d) The evidence shows it is unreasonable to expect that any plan of reorganization can be effected.

(1) **The Assignments of Error Made by Appellant in Its Appeal to the Circuit Court of Appeals Did Not Present Any Questions for Review.**

The appellant enumerated fifteen assignments of error in its appeal to the Circuit Court [Tr. of Rec., Vol. I, pp. 116-118], but not a single assignment of error was directed to any particular numbered finding of fact, nor was any particular numbered finding of fact challenged on the ground that it was not sustained by the evidence. Nor did the assignments of error set out separately and particularly each error asserted and intended to be urged. The assignments of error did not in any particular point out in what respect or for what reason the judgment of the United States District Court was claimed to be erroneous.

The assignments of error as found on pages 116-118 of Volume I of the Transcript of Record set forth fifteen assignments of error. We understand the rule to be that in considering the sufficiency of the assignments of error resort cannot be had to the briefs to enlarge them or to make them more particular. (*American Surety Co. v. Fischer Warehouse Co.* (C. C. A. 9), 88 Fed. (2d) 536.)

In *Krause v. Snyder*, 87 Fed. (2d) 723, the Eighth Circuit Court said in part:

“ . . . The purpose of an assignment of error is to point out to the appellate court what action or ruling of the lower court is complained of, and to indicate in what respect or for what reason the action of the court is claimed to be erroneous. The party complaining of the action of the lower court ‘must



lay his finger upon the point of objection and must stand or fall upon the case he made in the court below.' . . . We have often said that each assignment challenging the rulings of the court on the admissibility of evidence should contain the matter objected to, the objection, the ruling of the court thereon, with any exception allowed, and any further matter that may be carried into the record by reason of the ruling of the court on the objection. . . ."

In the said case of *Krause v. Snyder, supra*, the Court held the following assignments of error 5, 7, and 10 as being wholly insufficient and inadequate to present anything for review:

"5. The Court erred in rendering judgment for the plaintiff against the defendants in the sum of Sixty-nine Hundred and Ninety-one Dollars and fifty cents (\$6,991.50).

"7. The Court erred in refusing to credit defendants with the sums of money paid by the American Sand & Material Company to the plaintiff and credited on a note of the American Sand & Material Company to the plaintiff dated June 7, 1930, or successive renewals thereof.

"10. The Court erred in excluding from the evidence testimony of the witness Jamieson and more particularly testimony of the witness relating to his examination of the books and records of the American Sand & Material Company."

We submit that a comparison of the foregoing assignments, as well as those set forth in *American Surety Co. v. Fischer Warehouse Co., supra*, with the fifteen assignments of error made by appellant [Tr. of Rec., Vol. I, pp. 116-118] clearly discloses the same fatal deficiency.

We understand the rules of the Circuit Court to require that, when findings are made,

“ . . . the specification of error shall state as particularly as may be wherein the Findings of Fact and Conclusions of Law are alleged to be erroneous. . . .” (Rules of Practice of the United States Circuit Court of Appeals for the Ninth Circuit, Rule 20.)

The assignments of error respecting the admission or exclusion of evidence wholly failed to comply with the rules of the Circuit Court, in that the assignment of error failed to quote the grounds urged at the trial for the objection and the full substance of the evidence admitted or rejected, and failed to refer to the page number in the printed or typewritten transcript where the same might be found.

Thus both the Circuit Court and counsel for appellee were left to conjecture as to why any of the actions of the trial court herein were erroneous. For instance, the assignment of error No. 8 [Tr. of Rec., Vol. I, p. 117] is as follows:

“8. That the court erred in overruling the objections to the findings of fact and conclusions of law filed by the Security-First National Bank of Los Angeles, a national banking association.”

There is no objection to the findings of fact proposed by the Security-First National Bank, but merely amendments proposed thereto, and all of the assignments of error appear to fall within the rule laid down by *Wade v. Blieden* (C. C. A. 8), 86 Fed. (2d) 75, and followed by the Circuit Court in *American Surety Co. v. Fischer Ware-*

house Co., *supra*, where the Court said in regard to similar assignments of error:

"Assignments III, IV, and V amount to nothing more than a statement that the court should not have made the findings which it made, but should have adopted the findings proposed by the appellant. In other words, the appellant in his assignments of error asserts generally that the trial court made wrong findings and reached wrong conclusions, and invites this court to retry the entire case, without indicating to this court in such assignments in what respects and for what reasons the finding of fact and conclusions of law upon which the decree is based are erroneous. In a recent opinion of this court it was held that such assignments were 'a clear violation of rule 11 (now rule 23) requiring that assignment of errors shall "set out separately and particularly each error asserted and intended to be urged."' E. R. Squibb & Sons v. Mallinckrodt Chemical Works (C. C. A. 8), 69 F. (2d) 685, 687. See, also, Columbia Pictures Corp. v. Lawton-Byrne-Bruner Ins. Agency Co., *supra*."

This situation also seems to be covered by the language of the Court in *Woods v. Rains* (C. C. A. 8), 104 Fed. (2d) 137, where the Court says:

" . . . The defendants challenge the sufficiency of the assignments of error and contend that the same do not present any questions for review in this court. This court has stated repeatedly that the purpose of assignments of error is to point out to the appellate court the specific action or ruling of the lower court which is complained of as erroneous. *Wade v. Blieden*, 8 Cir., 86 F. 2d 75. The defendants further contend that the assignments of error have been abandoned by the plaintiff's failure to argue the same. Both of these contentions are well taken. . . ."

**(2) In the Absence of an Attack, the Findings of Fact Are Conclusive Upon an Appellate Tribunal.**

As the assignment of errors does not attack the findings, the appellant must be held to be satisfied therewith.

In the case of *Arn v. Dunnett*, 93 Fed. (2d) 634, at 638, the Court says, in part:

“ . . . The findings are supported by substantial evidence and under the frequently repeated rule of this court, they will not be disturbed on appeal. . . . ”

In the case of *Singletary v. General Motors Acceptance Corporation*, 73 Fed. (2d) 453, the Court says:

“ . . . It was incumbent on GMAC to show on its appeal to the Supreme Court that there was no substantial evidence upon which the judgment of the lower court could be upheld; for the trial was held before the judge of the superior court without a jury, and his finding upon conflicting evidence was conclusive. . . . ”

In the case of *Century Electric Co. v. United States*, 75 Fed. (2d) 589, the Court says, in part, at 592:

“ . . . Conceding, but without deciding, that the consent for the second trial was a waiver of the point made on the first trial that the question of the invalidity of the assessment was not open, it is sufficient to say that the trial court has, by its judgment on the second trial, found upon all the evidence adduced that there was a compliance with section 250(d), and that the assessment was valid. The evidence to sustain such finding was substantial, and the finding must, therefore, stand. . . . ”

In the case of *Sherman v. Bramham*, 78 Fed. (2d) 443, at 444, the Court says, in part, as follows:

“ . . . It is the well-established rule of this court that on an appeal in equity the findings of the trial judge, when he has personally heard the testimony, will not be disturbed unless clearly wrong. . . .”

Under the above authorities we submit that it is clearly the duty of the appellant to object specifically, by proper procedure, to each numbered finding with which it is dissatisfied, and then to point out to the Court wherein and why such finding is erroneous and not supported by substantial evidence. Upon its failure so to do, such finding becomes conclusive.

Thus, under the circumstances here existing, it is respectfully submitted that this appellate tribunal will not disturb any of the findings made by the trial court in this matter.

### **(3) The Evidence Sustains the Findings of Fact.**

Appellee is of the opinion that all of the findings of fact are amply sustained by the evidence presented to the trial court. However, as pointed out hereinabove, no finding of fact has been attacked by appellant on the ground that it was unsustained by the evidence. Appellee will not, therefore, burden this Court with a detailed recitation of evidence which goes to support each specific finding. Hereinafter in this brief, in appellee's argument, we will discuss the issues which appellee deems material, and will show that the findings on said material issues are amply supported by the evidence.

- (4) The Petition of Appellant and the Evidence Adduced in Support Thereof Fail to Show That the Proceeding Is Filed and Prosecuted in Good Faith as Required by Section 75 of the United States Bankruptcy Act.
- (a) THE PETITION FAILS TO DISCLOSE ANY PLAN OF REORGANIZATION OR POSSIBILITY OF EFFECTING THE SAME.

It is submitted that the petition for reorganization must contain allegations showing a need for a reorganization, and must allege facts showing that petitioner has a basis for expecting that a reorganization can be effected. If the petition fails to present any plan of reorganization, or show that one may be forthcoming which has a reasonable possibility of being effected, then the petition is insufficient.

In the case of *Manati Sugar Company v. Mock*, 75 Fed. (2d) 284, the Court says, in part, as follows:

"A receiver in equity was appointed for the debtor, and he is now in possession of its property. The petition filed alleges that the appellants 'propose \* \* \* a reorganization' of the debtor. The petitioners are the holders of \$14,000 principal amount of first mortgage twenty-year 7½ per cent sinking fund gold bonds of the debtor out of a total of \$5,500,900 principal amount of such bonds outstanding. They allege in their petition that the debtor is unable to meet its debts as they are maturing and have already matured; that a receiver in equity was appointed; that 'your petitioners propose that said debtor shall effect a reorganization pursuant to section 77B of an Act entitled: "An Act to Establish a Uniform Sys-

tem of Bankruptcy throughout the United States," approved July 1, 1898, and Acts amendatory thereof and supplemental thereto (hereafter referred to as the Bankruptcy Act).' They allege that the debtor has not filed a petition or answer under section 77B of the Bankruptcy Act (11 U. S. C. A., Sec. 207), and pray relief that an order be entered approving this petition as properly filed under section 77B, and that trustees of the estate of the debtor be appointed.

"The statute (section 77B, 48 Stat. 911, 912, c. 424 (11 U. S. C. A., Sec. 207)) authorizes any corporation, which may become a bankrupt under section 4 of the act, to file an original petition, 'stating the requisite jurisdictional facts under this section; the nature of the business of the debtor; in brief description, the assets, liabilities, capital stock, and financial condition of the debtor; if a prior proceeding is pending, the name of the court in which it is pending and the nature of such proceeding; facts showing the need for relief under this section; and that the corporation is insolvent or unable to meet its debts as they mature and that it desires to effect a plan of reorganization.

\* \* \* Three or more creditors who have provable claims against any corporation which amount in the aggregate, in excess of the value of securities held by them, if any, to \$1,000 or over may, if such corporation has not filed a petition or answer under this section, file with the court in which such corporation might file a petition under this section, a petition stating that such corporation is insolvent or unable to meet its debts as they mature and, if a prior proceeding in bankruptcy or equity receivership is not pending, that it has committed an act of bankruptcy within four months, that such creditors propose that it shall effect a reorganization; and such corporation shall, within ten days \* \* \* answer such petition.'

"The petition, like every petition in bankruptcy, should set forth the essential facts constituting the right to proceed in bankruptcy. In *re Fuller*, 15 F. (2d) 294 (C. C. A. 2); In *re Morosco Holding Co.* (D. C.) 296 F. 516. In addition to setting forth the jurisdictional requirements in the petition, there must be contained therein facts sufficient to satisfy the equitable obligations of good faith required by the statute, for the statute requires that the petition be filed in good faith. Whether the petition is filed by the debtor or, as here, by its creditors, the law requires the court to be satisfied that the petition has been filed in good faith. The court may be satisfied that the petition is filed in good faith in the absence of offer of proof to the contrary. But, in any case, the debtor or the creditors filing the petition have the burden of establishing good faith. In *re South Coast Co.* (D. C.), 8 F. Supp. 43; In *re Philadelphia R. T. Co.* (D. C.), 8 F. Supp. 51, affirmed November 19, 1934, 73 F. (2d) 1022 (C. C. A. 3).

"This petition does not set forth the present status of the corporation's affairs, its assets, its liabilities, or its equities above its first or other lien incumbrances, nor is a plan of reorganization set forth, nor a promise that one may be forthcoming. To conclude that a petition is filed in good faith, there should be a showing, found within it, of a need for a reorganization. The good-faith provision of the statute is not satisfied merely by honesty and good intentions. There must be a showing that the petitioners have a basis for expecting that a reorganization can be effected. Where the object is reorganization, rather than liquidation, the petitioner should furnish some assurance, by allegations at least, that they reasonably expect a fairly general support for their proposed plan or promised plan. Otherwise



there would be little to be expected in the undertaking of assuming responsibility for a reorganization.

"On the other hand, the honesty and integrity of the petition may not be questioned by the mere fact that petitioners' claims represent a small percentage of the claims against the debtor, if the aggregate of the claims is sufficient to come within the statutory requirements that Congress has determined to be sufficient to invoke relief under the act. The courts may not adopt any other test. But it must appear that there is reasonable probability that a reorganization will be effected. In other words, the question presented is whether there may be reasonably applied to the debtor some feasible and practicable plan of reorganization. If not, there is no occasion to invoke the benefits of the act.

"We do not mean to say that the petitioners cannot be heard unless they have a reorganization plan fully worked out and ready for immediate consideration, but it is essential sufficiently to show that one may be forthcoming. See *In Matter of 235 West 46th St. Co., Inc.*, 74 F. (2d) 700, decided January 7, 1935 (C. C. A. 2).

"The answers filed by the debtors and interveners, on the other hand, allege that no benefit will result to anyone from proceedings under section 77B, and such are the facts which are indicative of the impossibility of reorganization of the debtor. As set forth, the debtor produces sugar cane and manufactures raw sugar in Cuba. Its property consists chiefly of sugar plantations and a sugar mill, with administration offices and residential buildings, electric light plant, water supply system, and sewerage in the town of Manati, Cuba. It also has warehouses, boats, a shipyard, and a molasses tank. All of its property is

subject to a mortgage securing first mortgage bonds of \$5,500,900. There was a mortgage moratorium declared in Cuba on April 30, 1933, and no foreclosure proceedings may be instituted until July 1, 1935, and then only upon certain conditions. A receiver in equity was appointed February 9, 1932, and it has continued the business under the authority of the court, arranging for the necessary credit to do so. The interveners are a committee for the protection of holders of bonds, organized September 30, 1931. There has been default in the interest as well as principal. The debtor is without working capital, and is dependent upon bank loans. The price of sugar has been so low as to barely cover the cost of production, and it is alleged that the entire sugar industry is in a disorganized condition. Under these circumstances, the answers allege that no reorganization of the debtor at this time is possible. The District Judge said that he was not satisfied that the petition complied with section 77B and was not filed in good faith, as that term is used in the section.

"We think the petition was insufficient to comply with the requirements of this section and that it was properly dismissed.

"Order affirmed."

In the case of *Provident Mutual Life Insurance Company of Philadelphia v. University Evangelical Lutheran Church of Seattle*, 90 Fed. (2d) 992, the Court says, at page 995:

" . . . The purpose of the statute is to relieve distressed debtor corporations and to provide the mechanics for reorganization where reasonable expectation of continued useful existence may be fairly entertained. This being so, something more must be

demonstrated by the debtor than mere honesty or sincerity of purpose. If not, then the way is open to the exploitation of every involved corporation by visionaries whose illusory and optimistic imaginations outrun their business judgments, and the interest of every legitimate creditor is at the mercy of debtors whose sole hope of financial salvation is an abiding faith in miracles."

There is no reason to believe that the adoption of the Chandler Act has modified the holding in the above cases in any way, for the reason that section 130 of the Chandler Act provides:

"Every petition shall state . . . (6) the status of any plan of reorganization, readjustment, or liquidation affecting the property of the corporation, pending either in connection with or without any judicial proceeding; (7) the specific facts showing the need for relief under this chapter and why adequate relief cannot be obtained under Chapter XI of this Act; and (8) the desire of the petitioner or petitioners that a plan be effected."

The first seven paragraphs of appellant's petition for reorganization set forth the secured indebtedness owed by the corporation, the list of its stockholders, and the fact that the Security-First National Bank of Los Angeles had taken certain proceedings looking toward the liquidation of its secured indebtedness. [Tr. of Rec., Vol. I, pp. 5-21.]

In paragraph VIII it alleges its liabilities as of December 31, 1938, to aggregate approximately \$2,305,922.50, and its assets to be \$3,095,802.65, and refers to a financial statement of its assets and liabilities attached to the petition and marked Exhibit "A", and alleges that, in arriving

at the value of the parcels of real estate included in the assets of the corporation, the appraisals placed on substantially all of said real estate by Security-First National Bank of Los Angeles were used as a base for valuing the same. [Tr. of Rec., Vol. I, pp. 21-22.]

Paragraph IX alleges offers for said real estate made in 1929 and 1930. [Tr. of Rec., Vol. I, p. 22.]

Paragraph X alleges that additional legal proceedings will be immediately taken by the Bank of America National Trust and Savings Association and the California Bank and the Los Angeles Trust & Safe Deposit Company in respect to properties securing promissory notes, unless restrained by the Court, and will prevent appellant corporation from bringing into the Court a plan or plans of reorganization for the protection of said debts and creditors on some fair and equitable basis, for the purpose of conserving whatever equity appellant corporation may or can have in said real properties under any such plan. It is also alleged in said paragraph that if additional summary proceedings as provided under said trust deeds securing said indebtedness are begun, other small unsecured creditors will be influenced to bring other actions against appellant corporation, and that the present encouraging and improving business of appellant corporation will be forced into bankruptcy, and much of its real assets lost to the creditors and stockholders thereby. [Tr. of Rec., Vol. I, p. 23.]

Paragraph XI of the petition alleges in effect that values on Wilshire frontage are gradually increasing and in the opinion of appellant corporation will continue to increase in value, and that under a new plan of operation which appellant corporation proposes to submit the income of petitioner can be substantially increased so as to be able

to pay a fair rate of interest on the indebtedness of appellant corporation, and after some reasonable moratorium begin to pay something toward the amortization of the principal of said indebtedness. It is then further alleged that in the opinion of appellant corporation with improved world conditions it will be possible for it, by timely piecemeal sales of said properties, to pay off a substantial portion of said indebtedness and gradually liquidate the whole thereof, and thus save some equity for appellant corporation. There are then certain further allegations as to a World's Fair in 1939 in San Francisco, which should increase the income of appellant corporation's hotel property, and a further allegation that all hotels during the last several years have experienced a slump in business. [Tr. of Rec., Vol. I, pp. 23-24.]

Then appellant corporation, in paragraph XII, alleges payment of a large sum of interest to Security-First National Bank of Los Angeles over a period from approximately 1909, and that during September, 1937, Security-First National Bank of Los Angeles was paid \$294,782.33 by Charles C. Chapman on account of its indebtedness; that the hotel of appellant corporation has been conducted in the City of Los Angeles for approximately thirteen years, and during all of said period, even including the depression years, made fair profits from its operations, but now finds itself in respect of some of its other properties unable to pay its debts as they mature. It then alleges that, in view of recent developments in and near petitioner's properties, particularly on Wilshire boulevard, it has much brighter prospects than have existed for the last several years for the enhancement of the Wilshire frontage, and that the improvement of business conditions generally offers the prospect that enhancement of values

will place appellant corporation in a position of liquidating sufficient of their properties which, added to increased incomes therefrom with certain improvements made, will go to the point of paying off the creditors the amounts due and owing them as shown by the financial statement attached to said petition. [Tr. of Rec., Vol. I, pp. 24-26.]

In paragraph XIII it is alleged that the properties of appellant corporation must be conducted as a going business in its ordinary course or with some modifications in its present form to bring in a substantial income to service the loans against said properties, and that if said properties are caused to be sold or exposed to sale in lots or parcels at auctions or at forced, distress sale prices or in a manner other than a going business, then each and all of them would shrink in value and, under such conditions, it would become impossible to pay the creditors in full and would in such an event remove forever the possibility of conserving and saving any equity for appellant corporation. It is then alleged in said paragraph that petitioner throughout the years has developed a splendid credit; that it has a fine and large clientele. [Tr. of Rec., Vol. I, pp. 26-27.]

Paragraph XIV alleges that the appellant corporation can evolve a plan of reorganization that, in light of all the facts and circumstances, would be fair and equitable under the proceedings of said petition, by the terms of which the creditors in a reasonable period of time can be paid and the assets and good will of the petitioner be conserved and its business eventually profitably carried on. It is then alleged that appellant corporation has no money to offer any composition to creditors; that it desires, however, the opportunity to pay the creditors in full. It is

then further alleged in said paragraph that appellant corporation has offered proposals to its principal creditor, the Security-First National Bank of Los Angeles, by which the hotel properties solely would be turned over to the operator of a national chain of hotels, and under said proposal and under said operator's plan of operation the earnings would be so progressively increased as to eventually pay off the indebtedness, which said proposals the said Security-First National Bank of Los Angeles has refused to approve for acceptance. It is then alleged that in past years the appellant corporation has refused an offer of \$3,000.00 a front foot for the Brown Derby property, and that if perchance such values for Wilshire boulevard frontage should return, the 460 feet of frontage owned by petitioner could pay off at such a figure approximately \$1,380,000.00 in amount of said indebtedness. It is then further alleged (and Security-First National Bank of Los Angeles respectfully requests the Court particularly to note this allegation) that it is the belief of the appellant corporation that all of its creditors except the Security-First National Bank of Los Angeles have confidence that, if appellant corporation is permitted so to do, said appellant could work out of the present difficult situation if given adequate time. It is then further alleged that appellant corporation desires to pay off its debts in full and desires to effect a reorganization for the purpose of refinancing and thus be able to retain the good will of the Chapman name connected with said business, which it alleges it has created by years of continued operation in the community by a high standard of conduct. It is then alleged that the good will of appellant corporation is not included in its statement of assets, and that said good will is of great value. [Tr. of Rec., Vol. I, pp. 27-28.]



At the end of paragraph XVI of said petition it is alleged that appellant corporation desires to effect a plan of reorganization and extension under and pursuant to chapter X of the Chandler Act. [Tr. of Rec., Vol. I, pp. 30-32.]

We think it fair, in commenting upon the allegations of appellant corporation's petition herein, to make the statement that what appellant corporation is really asking is not a speedy, efficient reorganization, but a moratorium on its debts. The allegations of the petition indicate clearly that it does not hope to pay off its debts by reorganizing as a going business, but, on the contrary, by a liquidation of its properties by "timely piecemeal sales" thereof and by what it calls refinancing, together with what it hopes will be increased income.

Instead of alleging facts in its petition, the appellant corporation seems to find it necessary to allege its opinions or conclusions as to what will happen in the future. Examples of these allegations are such things as allegations that the values on Wilshire frontage are gradually increasing and, in the opinion of petitioner, will continue to increase; that the income of petitioner can be substantially increased; that with improved world conditions it will be possible, by timely piecemeal sales of the properties, to pay off a substantial portion of said indebtedness and gradually liquidate the whole thereof; that because there is a World's Fair in San Francisco the income of appellant's hotel property will be substantially increased; that in view of recent developments near petitioner's properties said properties appear to have a brighter prospect for enhancement of value, and that the improvement of business conditions generally offers the prospect that enhancement of values will place petitioner in a position of liqui-



dating sufficient of their properties which, added to the increased income therefrom, will go to the point of paying off the creditors the amounts due and owing them.

All of the allegations of the petition relative to any plan of reorganization or tending to show that it has such a plan have been hereinabove quoted, and it is respectfully submitted that at no point are any facts pleaded showing that a reorganization could be effected.

The allegations of the petition herein are utterly insufficient, in that they fail to allege facts sufficient to show the slightest possibility of a plan for reorganization that is at all practical or feasible or has the slightest chance of acceptance by a sufficient number of creditors to warrant proceedings under chapter X of the Bankruptcy Act. On the contrary, the allegations of appellant corporation's petition herein, in paragraph XIV thereof [Tr. of Rec., Vol. I, p. 28], show that the Security-First National Bank of Los Angeles has refused to approve other proposals of the petitioner and, further, has no confidence that the petitioner, if given time, could work out of the financial situation in which it finds itself. Further, the petition alleges facts which show that this creditor, the Security-First National Bank of Los Angeles, holds in excess of 60% of all outstanding indebtedness of petitioner, exclusive of the indebtedness owed to it as trustee. It thus is clear that, unless the consent of this creditor is obtained to a plan of reorganization, it cannot be accepted, inasmuch as section 179 of the Chandler Act requires that a plan of reorganization be accepted in writing by creditors holding two-thirds in amount of the claims filed and allowed in each class. It thus appears that the petition itself alleges facts which show that there was not a possibility of effecting a reorganization.

The allegations in said petition as to the future are opinions, and not facts. As was said in *Provident Mutual Life Ins. Co. of Philadelphia v. University of Evangelical Lutheran Church of Seattle*, *supra*, at page 995:

“ . . . The purpose of the statute is to relieve distressed debtor corporations and to provide the mechanics for reorganization where reasonable expectation of continued useful existence may be fairly entertained. This being so, something more must be demonstrated by the debtor than mere honesty or sincerity of purpose. If not, then the way is open to the exploitation of every involved corporation by visionaries whose illusory and optimistic imaginations outrun their business judgments, and the interest of every legitimate creditor is at the mercy of debtors whose sole hope of financial salvation is an abiding faith in miracles.”

- (b) THE APPELLANT CORPORATION'S LIABILITIES EXCEED ITS ASSETS TO SUCH AN EXTENT THAT IT SHOWS THE POSSIBILITY OF REORGANIZATION TO BE HOPELESS.

The one material issue of fact which seems to be in conflict is whether the value of the assets of the corporation exceeds or equals the liabilities of the corporation. The petition alleges that the corporation has a net worth of \$789,880.15. The answer controverts this allegation, and alleges that the appellant corporation is insolvent, and that its debts far exceed its assets. [Tr. of Rec., Vol. I, pp. 53-54.]

The major part of the testimony adduced at the trial concerned this issue. The Court resolved the issue in favor of the allegations contained in the answer of the

appellee, Security-First National Bank of Los Angeles, and found that the liabilities of the appellant corporation exceeded its assets by more than a million dollars. [Tr. of Rec., Vol. I, p. 85.] It is submitted that the evidence amply sustains the findings of the trial court on this issue.

Let us consider the evidence introduced by both sides on this question.

*Evidence of Appellant Corporation.*

The sole evidence as to values given on behalf of appellant was given by G. A. Chapman, its vice-president, who was not qualified as a real estate expert, and testified on the basis of being an officer of the corporation, the owner of the property. If it were not for this fact, his testimony would have been entirely inadmissible.

On cross-examination Mr. Chapman testified that his opinion as to the value of the property was based on an appraisal made by the Security-First National Bank of Los Angeles in 1934, together with his familiarity with the district and having lived there for thirty years or more. When he was asked what similar property was selling for in that area today, he answered that he was not in the real estate business, and was not familiar with any sales that had gone on around there. [Tr. of Rec., Vol. II, pp. 20-62.]

It seems to appellee that it is highly significant that appellant did not produce one single expert real estate appraiser.

*Evidence of Appellee.*

On the other hand, the appellee produced three expert real estate appraisers, who testified in connection with the value of the property of the appellant corporation.

One of these experts, Mr. Elon Brown, was an independent appraiser, not connected in any way with the appellee, Security-First National Bank of Los Angeles. Mr. Brown was fully qualified as an expert appraiser, and it is submitted that his testimony alone amply sustains the findings made by the Court regarding the present reasonable market value of the appellant corporation's properties. [Findings of Fact, XXI, Tr. of Rec., Vol. I, pp. 84-85.] The testimony of Mr. Brown is completely and fully set forth in the Transcript of Record, Volume II, pages 119-169.

Mr. Elon Brown is a real estate appraiser and general operator in real estate. For the past two years he has been employed by the Consolidated Hotels, in the capacity of appraiser for the purchase and sale of real property, such as hotels, apartment hotels, and apartments, in the county of Los Angeles, state of California. He has appraised numerous hotel properties in the county of Los Angeles in the past few years. He has been appraiser for the Occidental Life Insurance Company, Prudential Life Insurance Company, Metropolitan Life Insurance Company, State Highway Department of the State of California, Federal Home Loan Bank, and the Banking Department of the State of California. He has been continuously engaged in the real estate business in Los An-

geles since 1919. From 1927 to 1933 he had charge of all real estate and loan assets of the National Surety Corporation on the West Coast, covering the western states of Washington, Oregon, Idaho, California, Nevada, and Colorado.

During the period between March 10, 1939, and April 3, 1939, Mr. Brown made an appraisal of all of the properties of the Chapman Brothers Hotel Company, and has appraised the reasonable market value of the entire properties, including furniture and fixtures, at \$1,262,736.00. Mr. Brown's testimony considers each parcel of property in detail and covers 56 pages of the reporter's transcript, which are set forth in Transcript of Record, Volume II, pages 119-169.

Mr. Brown's testimony was supported by the testimony of Raymond F. Ahern and George F. Struble.

Raymond F. Ahern was called by appellee as another expert witness as to value on its behalf. He testified that he had been an appraiser of real estate for the Security-First National Bank of Los Angeles since 1926; that he was a graduate of the University of Nebraska in engineering, and had taken post-graduate work at the University of Southern California in appraisal courses and land economics; and that he was a member of the American Institute of Appraisers. That prior to the time he worked for the Security-First National Bank of Los Angeles he was a cost estimator for a local building contractor, and prior to that time was in the Engineering Department of the Union Oil Company in Los Angeles, designing various types of structures and estimating the cost of construction of buildings. That his duties in appraising for the Security-First National Bank of Los Angeles consisted of

evaluating various types of real estate, both city and country property.

That he had appraised the parcels of property numbered 1 to 18, those being the parcels securing the big loan of \$1,800,000.00, some of such appraisals having been made on October 18, 1938, and others having been made on January 23, 1939. Mr. Ahern's valuation of the 18 parcels of real estate showed that they were worth between \$450,000.00 and \$500,000.00 less than the debt which they secured. The detail of Mr. Ahern's testimony is to be found in the Transcript of Record, Volume II, pages 170-175.

On cross-examination Mr. Ahern testified that in arriving at the values he placed on these properties, he took into consideration the best uses to which they were adaptable. [Tr. of Rec., Vol. II, p. 175.]

The Court, after hearing the evidence produced by the parties to this proceeding, found that the value of the assets of the appellant corporation was over \$1,000,000.00 less than its admitted liabilities, and that the appellant corporation was hopelessly insolvent. The Court found as follows:

“XXI.

“That it is true that the present reasonable market value of the debtor's properties is as follows:

“(1) Properties securing indebtedness to Security-First National Bank of Los Angeles, a national banking association, in the principal amounts of \$1,800,000.00 and \$50,000.00, including the personal property covered by the chattel mortgage securing said loans, said property, with the exception of the personal property, being described in paragraph II of the answer of Security-First National Bank of Los

Angeles, a national banking association, on file herein, and in paragraph VI of these findings: \$996,514.00.

“(2) Property known as 516 South Alexandria avenue, Los Angeles, California, securing indebtedness to Security-First National Bank of Los Angeles, a national banking association, in the sum of \$9,087.61; \$8,375.00.

“(3) Properties securing indebtedness to Trust Department of Security-First National Bank of Los Angeles, a national banking association, as described in paragraph XIII of these findings:

Parcel 2—\$90,000.00

Parcel 1—\$30,835.00

“(4) Properties securing indebtedness to Bank of America National Trust and Savings Association, as described in paragraph XIV of these findings:

Parcel 1—\$15,600.00

Parcel 2—\$72,380.00

Parcel 3—\$33,372.00

“(5) Properties securing indebtedness to California Bank, a corporation, as described in paragraph XV of these findings: \$15,660.00.

“That it is true that the total present reasonable market value of all of the assets of the debtor corporation does not exceed \$1,300,000.00.

“That it is true that the debtor corporation admits a total liability on March 2, 1939, of \$2,319,339.49.

“That it is true that the liabilities of the debtor corporation exceed the assets thereof by a sum in excess of \$1,000,000.00, and the debtor corporation is hopelessly insolvent.” [Tr. of Rec., Vol. I, pp. 84-85.]

In addition to the actual finding on the reasonable market value of the appellant corporation's properties, the Court further found as follows:

“XXII.

“That it is true that on or about June 18, 1938, G. A. Chapman, vice president of debtor corporation, endeavored to induce Security-First National Bank of Los Angeles to exchange the real estate held by it as security for the promissory note in the principal sum of \$1,800,000.00 and the promissory note in the principal sum of \$50,000.00 for listed bonds which would liquidate at approximately fifty cents on the dollar of the indebtedness evidenced by said promissory notes, and at that time stated to said Security-First National Bank of Los Angeles that such bonds had better speculative value than the real property securing said loans.

“XXIII.

“That it is true that on or about October 31, 1938, C. Stanley Chapman, secretary-treasurer of debtor corporation, interviewed Security-First National Bank of Los Angeles, a national banking association, and at that time expressed himself as definitely of the opinion that said bank did not hold sufficient security for its indebtedness evidenced by said promissory note in the principal sum of \$1,800,000.00 and said promissory note in the principal sum of \$50,000.00 to pay out its claim, and that certainly no equity existed in said properties for debtor corporation. [Tr. of Rec., Vol. I, pp. 85-86.]

“XXIX.

“That it is not true, as alleged in paragraph VIII of debtor's petition herein, that the assets of the debtor corporation exceed its liabilities, but it is true, as more particularly hereinabove specifically found,



that the liabilities of the debtor corporation far exceed the present reasonable market value of its assets." [Tr. of Rec., Vol. I, p. 87.]

It is submitted that the findings above set forth are amply sustained by the evidence as found in the testimony of the witnesses, Elon Brown, Raymond F. Ahern and R. T. Adams. [Testimony of Elon Brown, Tr. of Rec., Vol. II, pp. 119-169]; testimony of Raymond F. Ahern, Tr. of Rec., Vol. II, pp. 170-175]; testimony of R. T. Adams, Tr. of Rec., Vol. II, pp. 176-199.] This testimony on behalf of appellee is the only testimony relative to a present reasonable market value of the properties of the appellant corporation, and that, we submit, is the question before the Court.

Appellee does not think it can be said that Mr. G. A. Chapman testified to any present reasonable market value; and what he thinks they were formerly worth, or what he hopes they could be sold for in the future under inflated circumstances or under more prosperous eras which the appellant corporation hopes will come about, is not a criterion of any present reasonable market value of the properties whatsoever. (*In re Pittsburgh Hotels Corporation*, 17 Fed. Supp. 949.) *Reading Hotel Corporation v. Protective Committee for First Mortgage Bondholders of Reading Hotel Corporation*, 89 Fed. (2d) 53, wherein the Court says, in part:

" . . . The hotel property, owned by the corporation, was subject to a first and second mortgage which, with accrued interest, in default, and taxes, netted some \$1,700,000, while the value of the property, with furniture added, was some \$1,300,000. It is quite evident that the stockholders have no equity and the bondholders have a right to foreclose . . .

"We recognize the fact that the hotel, under the admirable management of the appellant, has increased its gains steadily, and it may be that in the course of years such management might hereafter create an equity for the stockholders. But, in view of the fact that the mortgages are in default and the value of the property is several hundred thousand dollars less, the lienholders should not be compelled to await the possible outcome of the property, nor should they be compelled to accept a plan based on a R. F. C. loan effected on a mortgage by it which would have priority over their existing mortgage lien . . ."

(c) THE BURDEN OF PROOF TO SHOW A PLAN OF REORGANIZATION AND THE POSSIBILITY OF ITS BEING EFFECTED IS UPON APPELLANT, AND APPELLANT HAS FAILED TO SUSTAIN THIS BURDEN BY COMPETENT EVIDENCE.

Not only is it incumbent upon the petitioner to allege facts showing that the petition is filed in good faith as defined by Section 146 of the Chandler Act, but it is incumbent upon the petitioner to sustain the material allegations of his petition if the same be controverted by an answer filed in the proceeding. Upon the hearing of the issues raised by the petition and such answer, the burden of proof rests upon the petitioner.

In the case of *In re Cook*, 104 Fed. (2d) 981, answers were filed denying the essential allegations of the petition for reorganization. The matter was referred to a Master in Chancery, who heard testimony on the issues thus raised. The Court stated:

"The burden was upon appellees to sustain the allegations of the petition. *Hickey v. Ritz-Carlton Restaurant & Hotel Co.*, 3 Cir., 96 F. (2d) 748, 751."

In the said case the appellees were petitioners; in this case the petitioner is appellant.

In the case of *In re Hudson Coal Company*, 22 Fed. Supp. 768, the Court said, in part, as follows:

“The purpose of Section 77B of the Bankruptcy Act is to benefit the company and all persons in interest, and the burden is therefore on the petitioners for reorganization to establish their legal standing to institute the proceeding, their good faith, and the need for such reorganization. These questions lie at the threshold of the case before the Court should interfere with the affairs of the company. Such proceeding should be instituted in good faith either by the company itself or by the creditors for the benefit of the company. The questions of law that must be determined at the threshold of this case, therefore, are the standing of the creditor petitioners and their good faith.”

It is submitted that the appellant has not sustained this burden of proof and adduced evidence sufficient to support the material allegations of its petition. On the other hand, the appellee has adduced evidence in support of all of the allegations of the answer which controvert the material allegations of the petition.

(d) THE EVIDENCE SHOWS IT IS UNREASONABLE TO EXPECT THAT ANY PLAN OF REORGANIZATION CAN BE EFFECTED.

By specific legislative enactment it is required that a petition for reorganization shall be filed "in good faith." Further, by specific legislative enactment it is conclusively provided that under certain circumstances a petition shall be deemed not to be filed "in good faith." Section 146 of the Chandler Act provides as follows:

"Sec. 146. Without limiting the generality of the meaning of the term 'good faith,' a petition shall be deemed not to be filed in good faith if— . . . (3) it is unreasonable to expect that a plan of reorganization can be effected . . . ."

The question of good faith in the presentation of a plan or reorganization has been considered by the courts of the United States in the following cases:

In *Tennessee Publishing Co. v. American National Bank*, 299 U. S. 18, 57 S. C. 85, the Supreme Court of the United States said, in part, as follows:

"Nor do we need to inquire as to the precise limits of the concept of 'good faith' as required by section 77B. Whatever these limits may be, the statute clearly contemplates the submission of a plan of reorganization which admits of being confirmed as 'fair and equitable' and as 'feasible.' However honest in its efforts the debtor may be, and however sincere its

motives, the District Court is not bound to clog its docket with visionary or impracticable schemes for resuscitation. Sub-section (f) of section 77B provides for the confirmation of a plan only if the District Judge is satisfied '(1) that it is fair and equitable and does not discriminate unfairly in favor of any class of creditors or stockholders, and is feasible.' These are prime conditions. Unless the District Judge finds that the plan has these qualities he need go no further. Unless he so finds, he has no authority to proceed. There is no occasion for the District Judge to consider the constitutional validity of the application of the clauses of sub-section (b) (5) if the debtor's proposal is not found to be 'fair' and 'feasible.' It was the duty of the District Judge in this instance to consider the debtor's proposal in that aspect. He did not find that proposal to be fair and feasible. On the contrary, he deemed it to be unjust to the bondholders to override what had been accomplished in the equity case. He found that it was impracticable to determine the value of their bonds except by a public sale and, in view of the financial condition of the debtor, he deemed a sale of its property to be 'inevitable'. And along with these considerations, the proposal encountered what he described as the almost unanimous opposition of the secured creditors and the refusal of assent by a majority of the general creditors. Where the debtor's plan of reorganization is not confirmed the District Judge is authorized to dismiss the proceeding. Sub-section (c) (8)."

The Ninth Circuit Court of Appeals has followed this decision of the Supreme Court and quoted the above language in its decision in *Provident Mutual Life Ins. Co. of Philadelphia v. University Evangelical Luthern Church*

of *Seattle*, 90 Fed. (2d) 992, where Justice Denman, speaking for the Ninth Circuit Court, says:

“ . . . The next question concerns itself with the meaning of ‘good faith’ as stated in the statute.

“Good faith is more than *bona fide* intentions. The petition in order to satisfy this requirement must show some possibility of successful reorganization. In *Manati Sugar Co. v. Mock*, 75 F. (2d) 284, 285, the Circuit Court of Appeals for the Second Circuit said: ‘The good-faith provision of the statute is not satisfied merely by honesty and good intentions. There must be a showing that the petitioners have a basis for expecting that a reorganization can be effected.’

“The Sixth Circuit Court of Appeals expressed a like conclusion in *Re Tennessee Publishing Co. (C. C. A.)* 81 F. (2d) 463, 466: ‘We think it clear, however, in agreement with the Second Circuit, that something more than sincerity of intention was intended. The purpose of the statute is to relieve distressed debtor corporations and to provide the mechanics for reorganization where reasonable expectation of continued useful existence may be fairly entertained. This being so, something more must be demonstrated by the debtor than mere honesty or sincerity of purpose. If not, then the way is open to the exploitation of every involved corporation by visionaries whose illusory and optimistic imaginations outrun their business judgments, and the interest of every legitimate creditor is at the mercy of debtors whose sole hope of financial salvation is an abiding faith in miracles.’

“This case was affirmed by the United States Supreme Court on another ground. *Tennessee Pub. Co. v. American Nat. Bank*, 299 U. S. 18, 57 S. Ct. 85, 81 L. Ed. . . . . In the course of the opinion Chief

Justice Hughes stated (299 U. S. 18, 22, 57 S. Ct. 85, 87, 81 L. Ed. ....): 'Nor do we need to inquire as to the precise limits of the concept of "good faith" as required by section 77B. Whatever these limits may be, the statute clearly contemplates the submission of a plan of reorganization which admits of being confirmed as "*fair and equitable*" and as "*feasible*." However honest in its efforts the debtor may be, and however sincere its motives, the District Court is not bound to clog its docket with visionary or impracticable schemes for resuscitation.'

"These holdings completely resolve the issue of good faith against the debtor in the case at bar. A more visionary and hopeless scheme for financial rehabilitation could hardly be imagined. Exclusive of continuing interest, the debtor has obligations exceeding \$10,000, yet over the proposed five year plan of reorganization it plans to raise only a little more than \$6,000 and that from sources none too certain.

"But aside from the hopelessness of the proposition, the clogging of the docket 'with visionary or impractical schemes for resuscitation,' the petition sets forth a plan which beyond question would deprive the appellant of its property without due process of law. The plan gives appellant some three hundred dollars accrued interest, where it is entitled to more than twelve hundred. Whereas an interest rate to appellant of 6% per annum (greater on default) was contracted for, it is given in the future a rate of 2 per cent. Where it was entitled to total payment of its obligation in 1935, it is offered payment at a rate which will leave an amount still owing after a quarter of a century has elapsed since the date of the plan's confirmation. In the meantime, the debtor retains its

property, an unsecured creditor is paid in full, and various amounts are awarded to second mortgagees.

"In the words of the Supreme Court in the Tennessee Publishing Co. case, such a plan could not possibly admit 'of being confirmed as "fair and equitable" and as "feasible".' See *Louisville Joint Stock Land Bank v. Radford*, 295 U. S. 555, 594, 55 S. Ct. 854, 79 L. Ed. 1593, 97 A. L. R. 1106; *Security-First Nat. Bank v. Rindge Land & Nav. Co.* (C. C. A. 9) 85 Fed. (2d) 557, 561, 107 A. L. R. 1240.

"The order appealed from is reversed, and the District Court instructed to dismiss the petition as to appellant and in so far as it affects its mortgage.

"Reversed."

It is clear that the appellant corporation must allege facts in its original petition showing the offer or promise of a plan of reorganization that is feasible and expected to secure the general support of a majority of its creditors. In this regard the Court, in *Manati Sugar Company v. Mock*, *supra*, says:

" . . . This petition does not set forth the present status of the corporation's affairs, its assets, its liabilities, or its equities above its first or other lien incumbrances, nor is a plan of reorganization set forth, nor a promise that one may be forthcoming. To conclude that a petition is filed in good faith, there should be a showing, found within it, of a need for a reorganization. The good-faith provision of the statute is not satisfied merely by honesty and good intentions. There must be a showing that the petitioners have a basis for expecting that a reorganization can be effected. Where the object is reorganization, rather than liquidation, the petitioner should furnish some assurance,



by allegations at least, that they reasonably expect a fairly general support for their proposed plan or promised plan. Otherwise there would be little to be expected in the undertaking of assuming responsibility for a reorganization.

“On the other hand, the honesty and integrity of the petition may not be questioned by the mere fact that petitioners’ claims represent a small percentage of the claims against the debtor, if the aggregate of the claims is sufficient to come within the statutory requirements that Congress has determined to be sufficient to invoke relief under the act. The courts may not adopt any other test. But it must appear that there is reasonable probability that a reorganization will be effected. In other words, the question presented is whether there may be reasonably applied to the debtor some feasible and practicable plan of reorganization. If not, there is no occasion to invoke the benefits of the act.

“We do not mean to say that the petitioners cannot be heard unless they have a reorganization plan fully worked out and ready for immediate consideration, but it is essential sufficiently to show that one may be forthcoming. See *In Matter of 235 West 46th St. Co., Inc.*, 74 F. (2d) 700, decided January 7, 1935 (C. C. A. 2). . . .”

The appellant corporation’s plan of reorganization as alleged in the petition is summed up in the following allegation:

“XVI.

“That, as aforesaid, there is now authorized and outstanding 100,000 shares of capital stock of this corporation of a par value of \$1.00 per share. That

it is possible that your petitioner and its officers and directors, with the assistance of the trustees appointed hereunder and the co-operation of the creditors, subject to the approval of this court, that the said stock structure of your petitioner might be amended in accordance with the laws of the State of California so as to provide an issuance of bonds, accumulative preferred stock, callable at the election of the Board of Directors, at a premium and that when, as and if such amendment is approved by the court and the parties herein interested, that an appropriate petition therefor be secured from the corporation commissioner of the State of California to the end that said bonds and preferred stock in a sufficient amount with appropriate privileges and priorities, as is customary under the premises, be offered to the public and perhaps to the creditors of this corporation, all to the end that the indebtedness of the creditors herein could be eventually liquidated and paid. That under such suggested plan of reorganization your petitioner, if such plan is adopted, could hold its equities in the form of common stock and that no dividends could be declared thereupon until the retirement of said bonds and preferred stock at the earliest possible moment consistent with the earnings of your petitioner under an appropriate budget reserve set up from such earnings from time to time so as to enable said bonds and preferred stock to be retired in accordance with the said budgeting plan.

“Petitioner further represents that it is the opinion of your petitioner’s officers that petitioner’s business should be carried on in the interim by the receivers appointed by the Superior Court in action #433,394, in the Superior Court of the State of California, in and for the County of Los Angeles, entitled ‘Los

Angeles Trust and Safe Deposit Company, a corporation, and Security-First National Bank of Los Angeles, a national banking association, vs. Chapman Brothers Company, a corporation, *et al.*' as hereinafter prayed for, and that the foregoing plans, or additional plans submitted by the trustees appointed by this court be appraised so as to enable petitioner to continue in business, to keep currently paid all of its overhead obligations, same to be paid in accordance with the customs of business and trade practices, all obligations for the purchase of merchandise, and that during the period of administration of the affairs of this corporation under said trustees, plans for the reorganization of petitioner, subject to the approval of this court, with appropriate notices to, and co-operation of, petitioner's creditors, be given the closest study, providing for a priority of payment during said period of all taxes due to any governmental authority, and that during said time this Court and the trustees appointed by this honorable court retain jurisdiction of all proceedings hereunder after confirmation of a plan, if such eventuates, and until the indebtedness of this corporation, if need be, has been fully paid, satisfied and discharged . . . ." [Tr. of Rec., Vol. I, pp. 30-31.]

In addition to the foregoing allegation, the appellant corporation further alleges, in paragraph XI of its petition, as follows:

"XI.

"Your petitioner alleges that recently, within a short distance of your petitioner's Wilshire frontage, of which there is 460 feet belonging to your petitioner, there has been erected a de luxe building, to-wit, I. Magnin & Co., and that there has been estab-

lished within one and one-half blocks of your petitioner's Wilshire frontage, on Wilshire Boulevard, a Thrifty Drug Store, and that in the opinion of your petitioner, the values of said Wilshire frontage are gradually increasing and in the opinion of your petitioner will continue to increase in value and that generally said properties, under a new plan of operation which your petitioner proposes to submit, that the income of your petitioner can be substantially increased so as to be able to pay a fair interest rate on the indebtedness of your debtor and after some reasonable moratorium, begin to pay something toward the amortization of the principal of said indebtedness and that also, in the opinion of your petitioner, with improved world conditions, it will be possible for your petitioner by timely piece-meal sales of said properties, to pay off a substantial portion of said indebtedness and gradually liquidate the whole thereof and thus save some equity for your petitioner . . .” [Tr. of Rec., Vol. I, pp. 23-24.]

The sole evidence in support of the foregoing allegations in the petition was presented by Mr. G. A. Chapman, whose testimony in this respect consisted merely of recounting details of certain conversations and conferences that he had had with various people. All of these conferences had no definite, tangible result or conclusion whatsoever. [Tr. of Rec., Vol. II, pp. 62-118; and Tr. of Rec., Vol. I, pp. 139-161, 164-169.]

For instance, some conversation and correspondence was had with an operator of a national chain of hotels. As a matter of fact, Mr. Campbell, counsel for appellant corporation, wrote a letter (Exhibit “A” on behalf of Security-First National Bank of Los Angeles) to the Bank relative to this particular deal, and, among other

things, stated in substance that to the surprise of the appellant corporation the national hotel representative had stated comparative figures to the effect that the Wilshire frontage was worth \$700.00 to \$800.00 a front foot, and Alexandria frontage perhaps \$150.00, and so forth, and that the properties could be made worth a figure he had put upon them by his plan of operation. This plan of operation required extensive advertising, the installation of popular-priced dining rooms, de luxe cocktail rooms, orchestra and entertainment. This letter stated that Mr. Campbell tried to sell him the properties, but trying to make a sale to him and his chain at that time was hopeless. Buying it at any price was temporarily out of the question until their operating the properties made them worth something. Mr. Campbell further stated that, in the final analysis, that was right. This evidence is contained in two letters which were marked "Security-First National Bank's Exhibit 'A'." The letters are as follows:

"LAW OFFICES

"EVANS, PEARCE & CAMPBELL

"Wm. Harrison Campbell

"Albert D. Pearce

"William E. Evans

Suite 1010  
Pershing Square Building  
Los Angeles

December 12, 1938

"Security-First National Bank of Los Angeles

"Sixth and Spring Streets,

"Los Angeles, California

"Attention: Messrs. Austin and Adams

"Gentlemen:

"Following my last telephone conversation with your Mr. Adams, I had Burton Corporation wire the eastern prospect, of whom I spoke to Mr. Adams,

to come here immediately. On his arrival here, he made a very careful inspection of all the properties which interested him for his purposes and, from a real estate standpoint, stated, to our surprise, some comparative figures he had information about to the effect that Wilshire frontage was worth \$700 to \$800 a front foot, if developed; Alexandria frontage, perhaps, \$150, and so forth; and that the properties could be made worth a figure he had put upon them by his plan of operation.

"His chain is backed by millions of dollars, and his success in the operation of many similar properties furnishes a splendid yardstick. If this deal is entered into, the prospects purpose to do extensive advertising, install popular priced dining rooms, de luxe cocktail rooms, orchestra entertainment, etcetera.

"His searching size-up of what was needed, and its costs, were most revealing—in fact, I got the impression that within a couple of years or so they might enlarge the hotel or build another unit on the block.

"Of course, I tried to sell him the properties, but trying to make a sale to him and his chain at this time was hopeless. Buying it at any price was temporarily out of the question, as he pointed out—until their operating the properties made them worth something. Of course, in the final analysis, he is right.

"I am convinced the plan he finally proposed, which is set forth in the Burton letter herewith enclosed, is the only deal they will consider, and I am also convinced that it is the best deal for your bank.

"The prospects are interested only in the hotel block, the Brown Derby Frontage and the vacant

block between Normandy and Mariposa, and it is proposed that the XYZ Company pay out \$1,225,000 for these properties, as set out in the Burton letter. Frankly, this was a better deal than we had hoped, at the outset, to work out.

"May we have your best and promptest consideration and cooperation to the end that the details of this may be set up at once in a firm escrow and have him return here promptly on our telegraphic instructions for closing the same? I feel strongly, for several reasons, that this should be closed before the end of this month.

"Yours very truly,

"WM. H. CAMPBELL

"WHC:EH"      "Of EVANS, PEARCE & CAMPBELL."

[Tr. of Rec., Vol. II, p. 67.]

"128 South La Brea Avenue

"Los Angeles

"December 8th, 1938.

"Mr. William H. Campbell,  
"1010 Pershing Square Building,  
"Los Angeles, California.

"Dear Mr. Campbell:

"As you requested, we arranged for a conference yesterday in your office with an Eastern party who is a logical prospect for the solution of the problem of the Chapman Park Hotel. This letter will serve as a summary of that conference, and the detail of the conversation. This party is perhaps the most outstanding prospect for the solution of this problem that there is in the United States. The individual you met represents a hotel chain which operate many

hotels in several States. Their purchasing power alone makes possible unbelievable savings—for example, Chapman Park Hotel pays \$.80 per dozen for water tumblers that this organization buys for \$.36. They have, at present, tremendous following, and have out in the hands of the travelling public many thousands of credit cards. Our client has made a complete inspection of the property, and after a full and complete discussion of all of the possibilities, his plan is substantially as follows:

“That a new corporation be formed, which, for the time, we will call ‘XYZ Corporation.’ The title to the hotel property, including all Wilshire frontage, and the vacant piece on Sixth between Mariposa and Normandie, be conveyed to the XYZ Corporation subject to a new loan of \$1,225,000.00, the XYZ Corporation to be in effect a holding company of the operator. The XYZ Corporation will then execute a 15 year lease to a subsidiary corporation of the large hotel chain now operated by our client. Under this contract, one-third of the net profit will go to the subsidiary operating company, and two-thirds to the XYZ holding company. It is the present plan that the XYZ Corporation will give the subsidiary operating company an option to purchase the property at a price of \$1,225,000.00. The basis of this lease agreement would call for the servicing of the new encumbrance out of earnings before any net profit was established for distribution.

“Our client’s suggestions for the immediate increase in revenue and earning power, are to operate a more popular commercial type of hotel, the installation of a popular priced dining room, cocktail bars, entertainment features, etc., and for the later increase in revenue, the development of the Wilshire frontage with a drug store, exclusive shops, etc.



"We feel that everyone who has made any study of this situation will agree that this type of development is the only salvation of this property, and the only solution for the problem.

"As a real estate firm of many years' experience, we are confident that with the exceptional experience of successful management possessed by our prospect, together with the economies of operation, and increased revenues from improvements, the immediate income will be substantially increased to a point to make easy the servicing of the loan against the property, and the eventual exercising of the option to purchase.

"May we emphasize that our prospect has examined other properties on the Pacific Coast, and that we feel that we should give him a very prompt answer to his proposal.

"Yours very truly,

"BURTON CORPORATION

"By RAY A. BEARD."

[Tr. of Rec., Vol. II, pp. 70-71, 73-74.]

Mr. Chapman finally, on cross-examination, testified that no deal was ever consummated with the national hotel chain, and that no negotiations were pending at the present time with them. [Tr. of Rec., Vol. II, p. 74.] Mr. Chapman further testified that he never talked personally to Barney Goodman relative to the alleged deal with him. [Tr. of Rec., Vol. II, p. 114.] He further testified that he had never had any dealings with Barney Goodman, and that said alleged negotiations were never consummated. [Tr. of Rec., Vol. II, p. 114.]

Mr. Jonas, a witness called on behalf of appellant corporation, testified on cross-examination that he had talked to Mr. Goodman, but that Mr. Goodman did not represent to him that he was buying the property as an individual. When Mr. Jones was asked if Mr. Goodman was acting as a promoter, he said he didn't know what you would call it, but that he was not purporting to make the deal with his own resources. [Tr. of Rec., Vol. II, p. 200.]

Mr. R. T. Adams, an officer of the Security-First National Bank of Los Angeles, testified on direct examination by counsel for the appellant corporation that on approximately October 3, 1938, a Mr. Cason made an offer for Parcels 6, 7, 13, 14, 16 and 18, and all the personal property in the hotel and bungalow developments, at a figure somewhere between \$700,000.00 to \$800,000.00, and that the bank passed on an offer to Mr. G. A. Chapman and Mr. C. S. Chapman for a credit of \$1,000,000.00 less expenses, all cash, because the Bank felt there was a loss in the transaction. [Tr. of Rec., Vol. I, pp. 192-194.] This offer was made approximately October 3, 1938. This testimony shows the bank was then willing to take a loss on these properties of approximately \$250,000.00.

Mr. R. T. Adams further testified on direct examination that he had a conversation in his office with Mr. G. A. Chapman, Mr. Campbell, counsel for appellant corporation, and Mr. Lloyd L. Austin, another officer of the Bank, on or about October 26, 1938, in which a list of bonds with a highest speculative market value at that time of \$826,894.00 was offered to the bank in exchange for a complete release of the bank's loan of \$1,800,000.00 and the loan of \$50,000.00, both of which were secured

by the eighteen parcels of real property, and that at that time Mr. Chapman told the witness that the bonds had a greater speculative value than the real property which the bank was asked to release in exchange for them; that after the price situation had been discussed, Mr. Austin and the witness undertook to convince Mr. Chapman and Mr. Campbell that, in view of the fact that the bonds would liquidate for only approximately 50¢ on the dollar of the bank's investment in the real property, they could not justify an acceptance thereof from a banking standpoint. [Tr. of Rec., Vol. II, p. 178.]

Mr. Adams further testified that he had two conversations with Mr. C. Stanley Chapman, secretary-treasurer of the appellant corporation, the first of such conversations being on or about the 3d day of October, 1938, in the witness' office, and that Mr. G. A. Chapman, Mr. C. Stanley Chapman and Mr. Lloyd Austin were present, with the witness. That at such conversation a general discussion ensued as to the general value of the property included in the eighteen parcels, and that both C. Stanley Chapman and G. A. Chapman indicated at that discussion that they felt that \$1,000,000.00 was certainly all, if not more than, the property could normally be expected to liquidate for at that time. The second discussion took place in the witness' office about October 31, 1938, when Mr. C. Stanley Chapman, Mr. Sam Collins, Mr. Lloyd Austin and the witness discussed the proposed foreclosure and receivership proceedings. That at that time Mr. C. Stanley Chapman told the witness that there would be no opposition to the foreclosure at all, because of the fact that he was convinced that no equity existed to protect the indebtedness which they held against the Chapman Brothers Company. [Tr. of Rec., Vol. II, p. 180.]

Mr. Adams further testified that on or about the 2d day of November, 1938, he had a conversation at which Mr. G. A. Chapman, Mr. Campbell, Mr. Lloyd Austin and himself were present, and that at that time it was suggested that the bank take a quitclaim deed to the property in lieu of foreclosure, and that because of the long and difficult years that Mr. Chapman had put in in the service of the corporation, some small piece of property be eliminated from the transaction and given to Mr. Chapman for his personal assets. That at that time the witness stated that the bank did not feel that there was sufficient collateral to protect their claim, and would not do it. [Tr. of Rec., Vol. II, p. 182.]

Mr. Adams further testified that he had a conversation with Mr. G. A. Chapman and Mr. Campbell, in which the possibility of taking a proceeding under Section 77B of the Bankruptcy Act was mentioned, and that such conversation took place about October 26, 1938, in the witness' office, and that Mr. G. A. Chapman, Mr. Campbell, Mr. Austin, Mr. Randall Boyd, Mr. Roane Thorpe and the witness were present. The witness testified that after a discussion of considerable length of the bank's point of view that there was not sufficient collateral available to pay its claim without a substantial loss and, after a discussion of the corporation's inability to provide other assets, Mr. Campbell and Mr. Chapman expressed not only considerable disappointment, but discouragement in the future of the corporation. A discussion came up as to the possibilities of delay, in order that they could reorganize, in which Mr. Campbell stated that, in view of all the circumstances, of the very large percentage of the total debt of the corporation which the bank held, and the overwhelming percentage of its total secured debt

held by the bank, nothing but delay would result in filing a petition under Section 77B, or whatever the new chapter of the Bankruptcy Act is. At that time Mr. G. A. Chapman agreed that, if they couldn't get additional consideration from the bank without involving the entire transaction in the courts, the situation was so short of equity that it would not be anything but dilatory tactics, and would avail their organization nothing. [Tr. of Rec., Vol. II, pp. 183-185.]

Mr. C. Stanley Chapman, in his testimony on cross-examination, admitted that he had stated that no equity existed in the properties of the appellant corporation from which the Transcounties Corporation could recover its indebtedness. [Tr. of Rec., Vol. II, p. 201.]

In addition to the matters and things above set forth, the evidence, we submit, further shows that the Security-First National Bank of Los Angeles is in good faith of the opinion that the appellant corporation has no plan or possibility of reorganization which is practicable or feasible, and also shows that it holds approximately 90% of the admitted indebtedness of the appellant corporation, and is absolutely opposed to any and all plans of reorganization which the appellant corporation has nebulously hinted at in its petition and the evidence adduced in support thereof. What assurance, then, does this appellant corporation have of securing the consent of this creditor to any plan of reorganization? In the case of *Manati Sugar Company v. Mock*, *supra*, the Court says, in part:

“ . . . Where the object is reorganization, rather than liquidation, the petitioner should furnish some assurance, by allegations at least, that they reasonably expect a fairly general support for their proposed plan or promised plan. . . . ”

In this case the allegation of the petition with reference to this matter is as follows:

“That it is the belief of your petitioner that all of the petitioner’s creditors except the Security-First National Bank of Los Angeles, a national banking association, have confidence that if your petitioner is permitted so to do that this debtor could work out of the present difficult situation if given adequate time.” [Tr. of Rec., Vol. I, p. 28.]

By this allegation in their own petition the appellant corporation shows that it has no assurance of securing the support of 90% of its creditors on its admitted liabilities for any plan of reorganization.

It is further submitted that the evidence shows that the officers and representatives of the appellant corporation itself, prior to the filing of the petition herein, expressed themselves that a proceeding for reorganization would result only in delaying a foreclosure. [Tr. of Rec., Vol. II, p. 185.]

None of the evidence hereinabove set forth is contradicted.

It is submitted that, in the face of the evidence adduced at the trial of this matter, not only has the petitioner failed affirmatively to show the slightest possibility of any plan for reorganization and, by reason thereof, utterly failed to sustain its burden of proof, but that the evidence adduced by appellee affirmatively shows an utter impossibility of reorganization.

Further facts which show it is unreasonable to expect that a reorganization can be effected are as follows:

In finding No. XIX [Tr. of Rec., Vol. I, p. 81], the Court found that the appellant corporation, on March

2, 1939, had an unsecured indebtedness of \$29,808.76, and a secured indebtedness of \$2,289,530.73, excluding the question of liability presented by the payment of the guaranty of C. C. Chapman. The Court further found, in finding No. XVI [Tr. of Rec., Vol. I, p. 78], that the appellant corporation was indebted to the Security-First National Bank of Los Angeles in the total sum of \$2,091,489.84. It thus appears from the foregoing facts that the indebtedness owing to the Security-First National Bank of Los Angeles constitutes approximately 90% of the secured indebtedness of the appellant corporation. Even excluding the indebtedness owing to the Trust Department of the Security-First National Bank of Los Angeles, the said bank still holds approximately 73% of the secured indebtedness of appellant corporation.

In addition, the Court made this Finding of Fact, which stands unchallenged:

“XXXVII.

That it is true that since on or about the month of January, 1937, the officers of the Security-First National Bank of Los Angeles, a national banking association, and the officers of the debtor corporation have together conferred almost continuously relative to plans looking to the improvement of the financial condition of debtor corporation and its rehabilitation, and it is true that the Security-First National Bank of Los Angeles, a national banking association, has in good faith arrived at the opinion that no possible plan of reorganization can be effected by the debtor corporation which would accomplish even its partial rehabilitation, and it is true that the Security-First National Bank of Los Angeles, a national banking association, a secured creditor who holds more than two-thirds of the entire indebtedness of the debtor



corporation, has formed this opinion after thorough and careful analysis of the financial condition of the debtor corporation, looking towards a rehabilitation of debtor corporation." [Tr. of Rec., Vol. I, pp. 89-90.]

From the foregoing facts it appears that a creditor holding in excess of two-thirds of the entire indebtedness of the appellant corporation has, in good faith, after more than two years of almost continuous consultation with appellant corporation, arrived at the opinion that no possible plan of reorganization can be effected by the appellant corporation which would accomplish its rehabilitation. Inasmuch as the Bankruptcy Act, by Section 179, requires that a plan of reorganization be accepted in writing by creditors holding at least two-thirds of the claims filed, it appears clearly unreasonable to expect the appellant corporation herein to secure the consent of its creditor, Security-First National Bank of Los Angeles, to any of the nebulous plans of reorganization disclosed by the pleadings or the evidence herein.

This is a circumstance that has been considered by some of the courts ruling on similar cases. For instance, in *Manati Sugar Company v. Mock, supra*, the Court says:

" . . . The good-faith provision of the statute is not satisfied merely by honesty and good intentions. There must be a showing that the petitioners have a basis for expecting that a reorganization can be effected. Where the object is reorganization, rather than liquidation, the petitioner should furnish some assurance, by allegations at least, that they reasonably expect a fairly general support for their proposed plan or promised plan. Otherwise there would be little to be expected in the undertaking of assuming responsibility for a reorganization . . . ."



Additional evidence supporting the Court's finding that it would be unreasonable to expect a plan of reorganization to be effected is the following:

Finding XX of the trial court is as follows:

"XX.

That it is true that the debtor corporation has shown a continuing loss on its operations since the year 1933; that a schedule of such net loss after all charges is as follows:

1934	\$120,924.88
1935	111,279.43
1936	101,778.46
1937	132,317.30
For 14 months preceding March 2, 1939	140,957.76"
[Tr. of Rec., Vol. II, p. 84.]	

This finding of fact is supported by stipulation in open court [Tr. of Rec., Vol. II, pp. 201-204] for the years 1934, 1935, 1936 and 1937, and by the testimony of Mr. Blanton, the appellant corporation's auditor [Tr. of Rec., Vol. II, pp. 1-20], for 1938.

The same stipulation in open court supports the findings of the trial court, which are contained in paragraph VII on pages 70, 71, 72, 73 and 74 of Transcript of Record, Vol. I. These findings of fact show that the indebtedness of the appellant corporation to the Security-First National Bank of Los Angeles progressively increased from \$428,100.00 on December 31, 1925, to \$1,613,976.93 on March 15, 1939. The increase in this indebtedness and the continuance to operate at a loss of in excess of \$100,000.00 a year are further very strong evidence sustaining the finding of the trial court that it is unreasonable to expect a plan of reorganization to be effected.

### **Basis of Petition for Writ of Certiorari.**

Appellant has stated, on page 5 of its Petition and Brief in Support Thereof, that the grounds for its Petition for a Writ of Certiorari are that the Circuit Court decided an important question of federal law since the amendments to the national Bankruptcy Act in conflict with the principles of decisions of other Circuit Courts on the same matter, and in conflict with the applicable decisions of this Honorable Court. It is respectfully submitted that none of the cases cited by appellant tends to establish any conflict whatsoever between the decision of the Ninth Circuit Court of Appeals in this case and the cases cited by appellant.

The other ground upon which the appellant seeks a writ of certiorari is that since the amendment to the national Bankruptcy Act there have been no clear decisions of this Honorable Court as to the limits of the concept of good faith required by Section 146 of Chapter X, and that cases cited in appellant's brief show variations in interpretations of the rule prior to amendments, not only between the circuits, but within the same circuit. It is respectfully submitted that the case of *Tennessee Publishing Company v. American National Bank*, 299 U. S. 18, decides and lays down the rule for what may be the good faith or bad faith of a petitioner in a reorganization matter; and that there are no conflicts whatever in any of the cases cited by appellant relative to the meaning of good faith.

On page 12 of appellant's brief to this Honorable Court it urges the point that Section 146 of the national Bankruptcy Act means that a petition in all cases shall be deemed to be filed in good faith if it does not fall within

the negations contained in subdivisions 1 to 4 of said Section 146. In answer to this point we respectfully submit that said section specifically says that, without limiting the generality of the meaning of the term "good faith", a petition shall be deemed not to be filed in good faith if it falls within any of said subdivisions 1 to 4 of said section; and it is respectfully urged that the meaning of the term "good faith" was not meant to be limited to said four subdivisions of said section, it being expressly stated so in said Section 146; and that, in addition to this contention, the case at bar certainly falls under subdivision 3 of said section, which states that a petition is deemed not to be filed in good faith if "it is unreasonable to expect that a plan of reorganization can be effected".

We respectfully submit to this Honorable Court that appellant has not brought itself within subdivision 5 of Rule 38 of the Supreme Court of the United States; that there is no new or novel question to be decided by this Honorable Court; and that what counsel for appellant is asking this Court to do is not to decide a question of law, but to assume the duties of a trial court and make findings of fact.

### **Conclusion.**

In conclusion, the appellee submits that the record on appeal herein and the brief of the appellant do not present any questions for review by this Court; that the appeal to the Circuit Court was fatally defective by reason of the fatally defective assignments of error. On the other hand, the findings of fact made by the trial court amply support the judgment and order appealed from. Said findings of fact were not challenged in any particular as being unsupported by the evidence.

The evidence and the findings of fact of the Court, based thereon, show that Chapman Brothers Company, the appellant corporation herein, is a corporation whose capital stock is principally held by members of the Chapman family; that the petition herein was filed for the benefit of these stockholders; that the appellant corporation alleges that it desires a reorganization in order that it may preserve some equity in its properties for its stockholders. The findings of the Court show that the hope of preserving some equity must, in the last analysis, be nothing more than "an abiding faith in miracles", as stated in *Provident Mutual Life Insurance Company of Philadelphia v. University Evangelical Lutheran Church of Seattle, supra*, the properties of the appellant corporation having been found to be worth \$1,000,000.00 less than its indebtedness.

A reorganization is sought by the appellant corporation herein, not for the purpose of safeguarding any of the interests of its various classes of creditors; there was absolutely no showing in the petition or in the evidence that any creditor or class of creditors desired a reorganization; but in the hope of delaying the foreclosure of its properties, in the belief that improving business conditions in the future would enable the appellant corporation to sell its properties piecemeal and perhaps save some equity for its stockholders.

Contrasted to this hope and faith of the appellant corporation are the unembellished facts of past experience, which disclose that since 1934 the appellant corporation has operated at a loss of slightly in excess of \$100,000.00 a year; its indebtedness has increased; its interest on its indebtedness has accumulated; taxes on its property have been paid in some instances

by its secured creditors for their own protection; its officers have orally admitted the hopelessness of the situation; its largest secured creditor, the Security-First National Bank of Los Angeles, must accept and consent to any plan of reorganization in order that it may be effected, yet this creditor, with so much at stake, has for more than two years been in almost continuous consultation with the appellant corporation discussing plans looking to its financial rehabilitation. The Court has found that this creditor, in good faith, arrived at the opinion that no reorganization could be effected that would rehabilitate the appellant corporation.

We believe that the language of Chief Justice Hughes in the case of *Tennessee Publishing Co. v. American National Bank*, *supra*, aptly describes this appellant corporation:

“ . . . However honest in its efforts the debtor may be, and however sincere its motives, the District Court is not bound to clog its docket with visionary or impracticable schemes for resuscitation . . . ”

We also believe that this matter presents no question of a conflict of decisions or a new and novel point of law.

It is respectfully submitted that a writ of certiorari should be denied.

EDMUND W. PUGH,

ROANE THORPE,

*Counsel for Appellee, Security-First National Bank of  
Los Angeles, a national banking association.*

